No. 16,014

IN THE

United States Court of Appeals

For the Ninth Circuit

UNITED STATES OF AMERICA,
Appellant,

vs.

ASHBY O. STEWART, Executor of the Last Will and Testament of Mary W. Stewart, Deceased,
Appellee.

On Appeal from the Judgment of the United States District Court for the Northern District of California.

APPELLEE'S PETITION FOR A REHEARING.

GEORGE H. KOSTER,
300 Montgomery Street,
San Francisco 4, California,
Attorney for Appellee and Petitioner.

RICHARD W. GRAHAM,
300 Montgomery Street,
San Francisco 4, California,
Of Counsel.

FILED
JUL - 7 1959
PAUL P. O'BRIEN, CLERK

PERNAU-WALSH PRINTING CO., SAN FRANCISCO

Table of Authorities Cited

Cases

Pages

Commissioner of Internal Revenue v. Clise (CA 9, 1941) 122 F(2d) 998 5

Edwards v. Slocum, 246 U.S. 61 5

Ithaca Trust Co. v. U. S., 279 U.S. 151 5

In re Knight's Estate, 31 Wash.(2d) 813, 199 P(2d) 89 .... 4, 7

Leuthhold's Estate, 50 Wash.(2d) 869, 324 P(2d) 1103 ... 7

Rhodes v. Commissioner of Internal Revenue, 41 B.T.A. 62, aff'd. (CA 8, 1941) 117 F(2d) 509 6

U. S. v. Waechter, 159 F(2d) 963, aff'g. 98 F Supp. 960 ...4, 7, 8

Codes

Internal Revenue Code of 1939:

Section 810 3

Section 811(e) 6

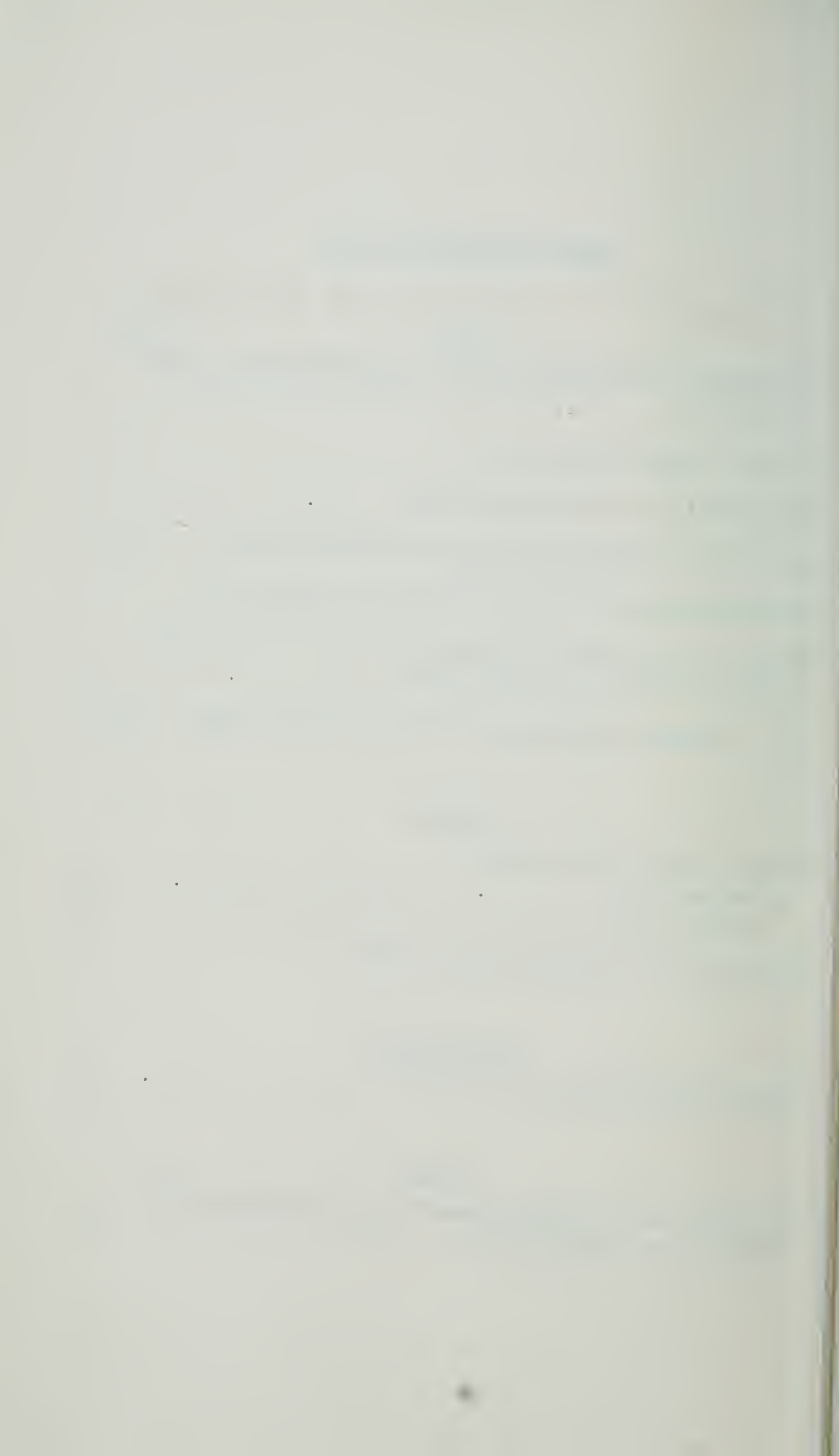
Revenue Code of California, Section 13401 3

Regulations

Treasury Regulations 80, Article 13 6

Texts

Beveridge, Law of Federal Estate Taxation (Callaghan & Co., 1956), Section 4.02, page 129 6



No. 16,014

IN THE

United States Court of Appeals

For the Ninth Circuit

UNITED STATES OF AMERICA, *Appellant,* vs. ASHBY O. STEWART, Executor of the Last Will and Testament of Mary W. Stewart, Deceased, *Appellee.*	}

On Appeal from the Judgment of the United States District Court for the Northern District of California.

APPELLEE'S PETITION FOR A REHEARING.

To the Honorable Judges of the United States Court of Appeals for the Ninth Circuit:

Petitioner, Ashby O. Stewart, Executor of the Last Will and Testament of Mary W. Stewart, deceased, the plaintiff-appellee above named, presents this, his petition for rehearing in the above-entitled cause, and in support thereof respectfully shows:

This Court in its decision on the issue as to whether any part of the value of insurance policies on the life of the surviving husband should be included in the

decedent's estate for federal estate tax purposes, acknowledged that this question "is determined by the State law of community property" (Opinion, p. 2). There is no California law which specifically defines or describes the nature or quantum of the wife's interest or estate at the time of her death in life insurance policies on the life of her surviving husband. However, there is such law now in the making through the medium of the case of *Estate of Mendenhall,* No. 56225, recently decided by the Superior Court of the State of California in and for the County of San Diego, which the State Controller has announced will be appealed.

This Court appears to be of the opinion that because the *Mendenhall* case involves the California Inheritance Tax law and because of differences between the California Inheritance Tax law and the Federal Estate Tax law, the ultimate decision in the *Mendenhall* case could not affect its decision here (Footnote 5 on page 6 of Opinion). It is respectfully submitted that the disposition of the issue in the *Mendenhall* case and in this case depends upon the same essential determination of the nature and extent of the wife's rights under California law in the insurance policies covering the life of her surviving husband.

Obviously then, if this case should reach the stage of finality before the final determination in the *Mendenhall* case, irreparable damage could result to the Stewart estate in the imposition of a substantial amount of non-refundable federal estate tax which might not be due, in the event the California Courts

should determine in the *Mendenhall* case that the wife had no interest in those policies which could be *transferred by or upon her death.*

The State inheritance tax is a tax imposed upon the transfer of property and for the privilege of receiving the property by succession;[1] the Federal estate tax is an excise tax imposed upon the transfer of property, and is for the privilege of transferring property.[2] It is significant that both laws require as a condition to the imposition of a tax that there be a "transfer" of property specifically subjected to the tax.

In the *Mendenhall* case the wife died leaving her estate in trust for her children. The California Inheritance Tax Department concluded that part of the property transferred by the wife by that bequest was her interest in life insurance policies covering the life of her surviving husband, and the Department thereupon asserted a tax against the beneficiary for the right to receive that bequest. The Superior Court determined that the wife had no interest in those policies which could be transferred by her either by Will or under the laws of succession, and the Court therefore concluded that there was no transfer and there could therefore be no inheritance tax. The Court states on page 1 of its opinion:

---

[1]Section 13401 of the Revenue Code of California: "An inheritance tax is hereby imposed upon every transfer subject to this part."

[2]Section 810 of the Internal Revenue Code of 1939: "A tax . . . shall be imposed upon the transfer of the net estate of every decedent citizen or resident of the United States dying after the date of the enactment of this title."

> "It is the opinion of the Court that at the time of her death the testatrix . . . had no such interest in the life insurance policies upon the life of her husband . . . as would result in a taxable transfer upon her death. . . ."

The significance of this decision is that if it is true under the California law that no one could obtain any interest in the insurance policies by transfer as a result of the wife's death, either under her Will or under the laws of succession, then there is no transfer of property upon which the tax can be imposed, whether that tax be a California inheritance tax or a Federal estate tax. It is the insurance contract which is the generating force directing the transfer of whatever interests may exist in the insurance policies. The death of any person mentioned in the contract may ultimately determine the person to whom the policy values will be transferred, but the death does not generate or effect the transfer. This principle was specifically invoked by the trial Judge in the *Waechter* case[3] in support of the conclusion that there could be no tax in the wife's estate with respect to the insur-

---

[3]In its decision in that case, at 98 F. Supp. 960, 962, the District Court said: "In the case of policies payable on the death of an insured, who is the surviving spouse, 'nothing whatever became payable on the death of the beneficiary, the deceased wife'. In re *Knight's Estate, supra*, 31 Wash(2d) at page 941, 199 P.2d at page 94. The language just quoted was used in a case arising under the inheritance tax statute of the State of Washington. But the logic of the reasoning applies with equal force to the estate tax. To be taxable, a transfer of an estate must occur. And if, as it appears, the wife had no power to transfer one-half of her surrender value in the policy, and upon her death nothing became due to her heirs, there is no interest to which the estate tax would attach. . . ."

ance policies covering the life of the surviving husband.

This Court throughout its opinion emphasizes the fact that the wife had an interest in the policies during her lifetime, and it is primarily on the basis of this premise that the Court finds "accordingly that a substantial interest passed from the wife to the husband upon the wife's death with respect to all of the policies" (Opinion, p. 10). Unless the term "passing" is used synonymously with the term "transfer", neither the Federal estate tax nor the California inheritance tax would be applicable. This Court cited *Commissioner of Internal Revenue v. Clise* (CA 9, 1941) 122 F(2d) 998, 1001, calling attention to the statement therein concerning the Federal estate tax, that "It does not tax the interest to which the legatees and devisees succeed on death but the interest which ceased by reason of death; what is imposed is an excise upon the transfer of an estate upon death of the owner." (Opinion, p. 6).

The first clause of the quoted statement[4] must be read in conjunction with the second clause, so that the reference to taxation of the interest which ceased by

---

[4]It would appear that in the case of *Commissioner v. Clise,* 122 F.2d 998, and other cases, the use of the clause that the taxing act taxes "not the interest to which some person succeeds on a death, but the interest which ceased by reason of the death", was intended to explain that once having established a taxable transfer the tax applied to the value of the property which was the subject of the transfer at the time of death, rather than some other value based upon what the legatees received. *Edwards v. Slocum,* 246 U.S. 61. In the case of *Ithaca Trust Co. v. U.S.*, 279 U.S. 151, the Supreme Court touches upon this situation with the remark, "The tax is on the act of the testator not on the receipt

reason of death must contain the further requirement that the interest which ceased by reason of death must also be the subject of a transfer by reason of the death and generated by the death. If it were not so, then such interests as life interests which ceased by reason of death would be subject to tax, and yet there is no question but that there is no tax upon the estate of a life tenant by reason of the termination of the life tenancy, notwithstanding that the interest of the remainderman becomes enhanced upon the death of the life tenant.[5] This is also true in the case of an interest which is contingent upon survival of a certain person or event, and no tax would be imposed upon that contingent interest if the person having it dies before the specified time, notwithstanding someone else has an interest which is immediately augmented by that death.[6] A similar situation exists in the case of joint tenancies, with respect to which a specific section in the law was considered essential to impose the estate tax.[7]

We believe that the logic and legal theory upon which the decision of the Superior Court in the *Mendenhall* case is predicated is that upon her death, the wife's property rights under the insurance contracts

---

of property by the legatees. *Young Men's Christian Assn. v. Davis,* 264 U.S. 47; *Knowlton v. Moore,* 178 U.S. 41; and passim; *New York Trust Co. v. Eisner,* 256 U.S. 345, 348, 349; *Edwards v. Slocum,* 264 U.S. 61."

[5]*Rhodes v. Commissioner of Internal Revenue,* 41 B.T.A. 62, aff'd, (CA 8, 1941) 117 F(2d) 509.

[6]Regulations 80—Article 13.

[7]Internal Revenue Code of 1939, Sec. 811(e); see Beveridge, *Law of Federal Estate Taxation* (Callaghan & Co., 1956), Sec. 4.02, p. 129.

were not the subject of a disposition or transfer but merely terminated or expired, and that she had nothing over which she had the right to exercise a power of disposition or transfer upon her death.

The Superior Court follows the reasoning of the case of *In re Knight's Estate,* 31 Wash.(2d) 813, 199 P.(2d) 89, specifically preferring it to the later decision of the Washington Supreme Court in the case of *Leuthhold's Estate,* 50 Wash.(2d) 869, 324 P.(2d) 1103. If by affirmance by the appellate courts the *Mendenhall* case should become the law in California on this subject, then the decision of this Court in the case of *U. S. v. Waechter,* 159 F(2d) 963, aff'g. 98 F. Supp. 960, *would be directly applicable* and under authority of the *Waechter* case the imposition of the Federal estate tax against Mrs. Stewart's estate on an alleged transfer of her interest in the policies would be wrong.

We hope that we have impressed the Court with our representations and argument contained herein, but whether or not we have impressed the Court sufficiently to warrant a modification of its decision and an affirmance of the District Court, we cannot in good conscience ask this Court to do more at this time than to defer action on this Petition until the appellate court has reviewed the *Mendenhall* case. We believe the final determination in the *Mendenhall* case must necessarily establish California law, which will be determinative of the question as to whether the wife's interests in insurance policies covering her surviving husband's life were of such a nature that they could

be evaluated and subjected to federal estate taxes as part of her gross estate, and as to whether this Court's decision in the *Waechter* case is applicable.

Wherefore, upon the foregoing grounds, it is respectfully urged that this petition for rehearing be granted and that upon further consideration the judgment of the District Court be affirmed in its entirety.

Dated, July 6, 1959.

Respectfully submitted,

GEORGE H. KOSTER,
Attorney for Appellee and Petitioner.

RICHARD W. GRAHAM,
Of Counsel.

Certificate of Counsel

I, George H. Koster, attorney for the petitioner herein, do hereby certify that in my judgment the foregoing petition is well founded and is not interposed for the purpose of delay.

Dated, July 6, 1959.

George H. Koster.